

General Information Letter: Petition to use separate accounting method cannot be granted absent a showing that the statutory apportionment method fails to fairly represent the business activities of the taxpayer in Illinois and that the separate accounting method does fairly represent business activities in Illinois.

February 16, 2000

Dear:

This is in response to your letter dated December 2, 1999, in which you request permission for xxxxxxxxxxxxxx to use an alternative method of apportionment under the provisions of Section 304(f) of the Illinois Income Tax Act (the "IITA"; 35 ILCS 5/101 et seq.). I apologize for the delay in responding to you. The nature of your letter and the information you have provided require that we respond with a General Information Letter, which is designed to provide general information, is not a statement of Department policy and is not binding on the Department. See 86 Ill. Adm. Code 1200.120(b) and (c), enclosed. For the reasons discussed below, your request cannot be granted at this time.

In your letter you have stated the following:

This petition is filed by xxxxxxxxxxxxxx to use an alternative apportionment method to allocate income to Illinois beginning with the 1998 tax year.

xxxxxxxxxxxxxx (a California S corporation) consists of two distinct and separate activities. Activity number 1 is providing the loan-out acting services of its sole shareholder. The sole shareholder is not an Illinois resident. Activity number 2 is ownership of a partnership interest engaged in automobile racing and the related expenses.

In 1998 none of the acting services were performed in Illinois and 100% of the automobile racing activity is being considered Illinois.

The only method that results in a correct allocation is a separate accounting for the two activities. This is relatively easy to do because for both activities the income and expenses are distinct. This petition is being filed as an attachment to a Form IL-843 for 1998.

In telephone conversations and subsequent correspondence, you have indicated that the outcome you are requesting is that xxxxxxxxxxxxxx be allowed to allocate to Illinois over \$300,000 in expenses it incurred to offset its \$1,734,075 share of the business income apportioned to Illinois by xxxxxxxxxxxxxxxxxxxxxx, a partnership in which xxxxxxxxxxxxxx owns a 44.74% partnership interest.

Response

For a corporation that is a partner in a partnership, there are two different ways to report the corporation's share of the partnership's business income. Under Section 305(a) of the IITA, the partnership apportions its income to Illinois using the appropriate formula under Section 304 of the IITA, and the partner includes its share of that income in its Illinois net income. The corporation apportions its own business income using the appropriate formula under Section 304 of the IITA.

However, when the corporate partner is engaged in a unitary business with the partnership, 86 Ill. Admin. Code Section 100.3380 provides that:

the partner's share of the partnership's income and factors shall be combined with the business income and factors of the partner or with the combined business income and factors of the unitary business group including the partner, as the case may be.

From the facts you describe in your letter and the supplementary materials you have provided, it appears that xxxxxxxxxxxxxx and xxxxxxxxxxxxxxxxxxxxxx may be engaged in a unitary business. If that is not the case, the expenses incurred by xxxxxxxxxxxxxx cannot be attributed to its income derived from xxxxxxxxxxxxxxxxxxxxxx, and there would be no basis for xxxxxxxxxxxxxx to allocate any of its expenses to Illinois. Thus, in the absence of a unitary business, you have given no reason sufficient to allow some of the expenses of xxxxxxxxxxxxxx to be allocated to Illinois, and your petition must be denied.

If xxxxxxxxxxxxxx and xxxxxxxxxxxxxxxxxxxxxx are engaged in a unitary business, xxxxxxxxxxxxxx must combine its share of the business income of xxxxxxxxxxxxxxxxxxxxxx with its business income and its share of the apportionment factors of xxxxxxxxxxxxxxxxxxxxxx with its own apportionment factors for use in apportioning that business income to Illinois. Only after this has been done can we determine whether or not the business income of xxxxxxxxxxxxxx apportioned to Illinois properly reflects its business activities in Illinois.

xxxxxxxxxxxxxxxxxxx reported no base income on its Illinois income tax return because all of its income is distributable to partners subject to replacement tax. Accordingly, it reported no information regarding its apportionment factors. As a result, we are unable to do the apportionment computations for you to determine what the tax liability of xxxxxxxxxxxxxx should be under the normal apportionment method, much less determine whether or not that liability is excessive and requires adjustment under Section 304(f). We therefore cannot grant your petition at this time.

In order to further pursue your request, it will be necessary for you to obtain the apportionment factor information from xxxxxxxxxxxxxxxxxxxxxx and use it to complete a Form IL-1120-ST in compliance with 86 Ill. Admin. Code Section 100.3380(c). If the resulting liability properly reflects the business activity of xxxxxxxxxxxxxx and xxxxxxxxxxxxxxxxxxxxxx in Illinois, submit that return with the supporting information with a new refund request. If it does not, please supplement your petition with the information from the Form IL-1120-ST and an explanation of why the prescribed method of apportionment fails to accurately represent xxxxxxxxxxxxxx business activities in Illinois, and we will reconsider it. A copy of 86 Ill. Admin. Code Section 100.3390 is enclosed for your reference in supplementing your petition.

As stated above, this is a general information letter which does not constitute a statement of policy that applies, interprets or prescribes the tax laws, and it is not binding on the Department.

Sincerely,

Paul S. Caselton
Deputy Chief Counsel -- Income Tax